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No. _____

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

HOUSTON LIGHTING AND POWER COMPANY,

Petitioner,

v.

THE HONORABLE JOSEPH B. MORRIS, JUDGE
(CITY OF SAN ANTONIO AND CENTRAL POWER
AND LIGHT COMPANY, REAL PARTIES IN INTEREST)

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF TEXAS

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January 27, 1992

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QUESTIONS PRESENTED FOR REVIEW

1. Whether a state court denies due process of law when it requires a defendant to submit to arbitration of claims against it by majority vote of a panel, when the panel majority has been appointed by the plaintiffs.

2. Whether a state court denies due process of law when it refuses to take any of several available actions before the arbitration begins to create an arbitration panel which is unbiased both in fact and in appearance.

3. Whether judicial review after an arbitration award under a standard which requires a showing of "evident partiality" or "corruption" for vacation is an adequate remedy to correct structural bias of an arbitration panel.

LIST OF PARTIES

Houston Lighting & Power Company

Petitioner

City of San Antonio, Texas, acting by and through
City Public Service Board of San Antonio
Central Power and Light Company
City of Austin, Texas[1]
Honorable Joseph B. Morris, Judge of the
101st Judicial District Court of
Dallas County, Texas[2]

Respondents

RULE 29.1 STATEMENT

Houston Lighting & Power Company ("HL&P") is a wholly owned subsidiary of Houston Industries, Inc., which is a publicly held company. Central Power and Light Company ("CPL") is a wholly owned subsidiary of Central and Southwest Corporation, which is a publicly held company.

[1] The City of Austin was not a party to the state district court proceedings but, at Austin's request, was named as a party in interest when HL&P sought review by mandamus in the Texas appellate courts.

[2] As presiding judge of the 101st Judicial District Court of Dallas County, Judge Morris made the rulings which are the subject of this Petition. Under Texas mandamus procedure, he was named as a formal respondent in the ensuing mandamus proceedings in the Texas appellate courts, but has no interest in the subject matter.

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IN THE

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OCTOBER TERM, 1991

HOUSTON LIGHTING AND POWER COMPANY,

Petitioner,

v.

CITY OF SAN ANTONIO AND CENTRAL POWER AND LIGHT COMPANY

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE DISTRICT COURT OF DALLAS COUNTY, TEXAS 101ST JUDICIAL DISTRICT

Petitioner Houston Lighting & Power Company ("HL&P") respectfully prays that a writ of certiorari issue to review the orders of the District Court of Dallas County, Texas, 101st Judicial District, entered August 22, 1990 and April 22, 1991, which (a) deny HL&P's due process rights by requiring it to submit to arbitration of claims against it by the City of San Antonio ("San Antonio") and Central Power and Light Company ("CPL") before a panel controlled by the appointees of the claimants against HL&P, and (b) deny HL&P's request for actions which, if taken, would have enabled the arbitration proceeding to meet applicable due process requirements. The Texas appellate courts had discretion to review the district court's action by mandamus but have refused to do so.

OPINIONS BELOW

The order of the District Court of Dallas County requiring arbitration dated August 22, 1990 (Appendix A) and the order denying relief in aid of fair arbitration dated April 22, 1991 (Appendix B) are not reported. The order of the Texas Court of Appeals at Dallas denying leave to file mandamus dated April 25, 1991 (Appendix C) is not reported. The order of the Texas Supreme Court dated June 19, 1991 denying leave to file mandamus (Appendix D) is reported at 34 Tex. Sup. Ct. J. 668, and the order of the Texas Supreme Court dated October 30, 1991 denying rehearing (Appendix E) is reported at 35 Tex. Sup. Ct. J. 61.

JURISDICTION

This Court has jurisdiction under 28 U.S.C. § 1257 (3).

HL&P resisted the orders of the district court on the ground that they violated HL&P's rights under the Fourteenth Amendment to the United States Constitution, and repeated this challenge in the Texas appellate courts, thereby preserving for review the constitutional questions presented. The denial of mandamus review by the Texas appellate courts makes the district court's order the decree of the highest Texas court for purposes of this Petition. *See, e.g., Minneapolis, St.P. & S.S.M. Ry. Co. v. Rock*, 279 U.S. 410 (1929).

Should HL&P's efforts to obtain review by mandamus not toll the running of the 90-day deadline imposed by 28 U.S.C. § 2101(e) for the filing of petitions for writ of certiorari, then HL&P respectfully requests the Court to treat this Petition as a request for certiorari review of the Texas Supreme Court's orders denying mandamus relief. These orders have the same effect as the district court's order. A state appellate court's refusal to entertain an original proceeding filed in that court qualifies as a "final judgment or decree" reviewable by certiorari. *See, e.g., Michigan Central Ry. Co. v. Mix, Mo.*, 278 U.S. 492 (1929).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The Fourteenth Amendment to the Constitution of the United States provides, in relevant part:

> [N]or shall any State deprive any person of ... property, without due process of law ....

Relevant portions of the Texas General Arbitration Act, Tex. Rev. Civ. Stat. Ann. art. 224 et. seq. (the "Texas Act"), and the Federal Arbitration Act, 9 U.S.C. § 1 et. seq. (the "FAA"), are reprinted as Appendix G and H, respectively.

STATEMENT OF THE CASE

In 1973 four electric utilities in Texas agreed to construct and operate jointly a two-unit nuclear power plant known as the South Texas Project ("STP") and executed a Participation Agreement to govern this undertaking. The four Participants are the City of San Antonio, acting by and through the City Public Service Board of San Antonio ("San Antonio"), the City of Austin ("Austin"), Central Power and Light Company ("CPL") and Houston Lighting and Power Company ("HL&P").[3] Relevant excerpts from the Participation Agreement are reprinted as Appendix I.

The Participation Agreement created a Management Committee composed of a representative of each Participant, which met regularly and made decisions concerning STP on the basis of the vote of Participants having an ownership interest greater than 60%; thus decisions required approval of at least three Participants. HL&P was designated Project Manager to make reports and recommendations to the Management Committee.

Before construction, it was estimated by consultants that STP would cost approximately $1 billion and be completed by 1982.

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[3] The interests in STP are owned by the four Participants as co-tenants in the following percentages: San Antonio (28%), Austin (16%), CPL (25.2%), and HL&P (30.8%).

In common with other nuclear projects of this era, construction cost escalations and delays were experienced at STP, due in large part to regulatory changes after the accident at the Three Mile Island nuclear plant. STP is now fully completed and operating; Unit One began commercial operation in 1988 and Unit Two in 1989. The final construction cost was $5.4 billion.[4]

Austin sued HL&P, claiming that the alleged failure by HL&P to perform its duties as Project Manager had increased STP construction costs by hundreds of millions of dollars. HL&P later joined San Antonio and CPL as parties in Austin's action. San Antonio and CPL then asserted their own claims against HL&P for damages comparable to those asserted by Austin, and demanded arbitration of the following global issues:

> [t]he extent to which Houston Lighting & Power Company has breached its obligations to [San Antonio and CPL] under the Participation Agreement, and the laws and statutes of the State of Texas, and the amount of statutory, actual and punitive damages caused by any such breach . . . .

No arbitration demand was made as to Austin's claims, and the claims of San Antonio and CPL were severed into a separate cause. Austin's claims were tried in 1989, and a jury found that the cost of STP had not been increased by any failure of HL&P to perform its duties as Project Manager. Judgment was entered denying Austin's claims against HL&P.[5]

After the *Austin* verdict San Antonio and CPL renewed their arbitration demands, basing them on the provisions of Section 23 of the Participation Agreement.[6] They insisted that each STP

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[4] After credit for a $750 million settlement paid to the Participants by Brown & Root, Inc., the original architect, engineer and constructor.

[5] Austin's appeal from this judgment is now pending decision in the Texas Court of Appeals at Dallas.

[6] Section 23.1 of the Participation Agreement permits a call for arbitration "If a dispute (other than as to a decision made [by the Management Committee] under Section 9.4 hereof) between any of the Participants should arise under this Participation Agreement." (App. 20a).

Participant is entitled to appoint one arbitrator under Section 23.2 and that accordingly their claims were to be decided by a panel of three arbitrators, one being appointed by each of San Antonio, CPL and HL&P.[7] Alternatively, if Austin was found entitled to appoint one of the arbitrators, then San Antonio and CPL asserted that the panel would be composed of four arbitrators, one each appointed by San Antonio, CPL, Austin and HL&P, respectively, and a fifth elected by the four.

HL&P strongly contested these arbitration demands, contending that Section 23 of the Participation Agreement did not contemplate, much less require arbitration of claims of this type, and that in any event arbitration by a panel controlled by the claimants was unfair and violated HL&P's constitutional and statutory rights. HL&P asserted that arbitration provisions were placed in the Participation Agreement as a means of resolving deadlocks on the Management Committee when a 60% vote could not be achieved, and were not intended as a vehicle for overturning Management Committee decisions on the basis of hindsight.[8] Nor were the arbitration provisions intended to be misused as a device for reallocating the agreed division of STP costs through recovery of damages from one Participant by other Participants.[9]

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[7] Section 23.2 (App. 21a) provides in pertinent part: "Any Participant calling for arbitration shall . . . [name] one arbitrator. [E]ach additional Participant . . . may appoint one additional arbitrator. If necessary to make the total number of arbitrators an odd number, the arbitrators so appointed shall elect one additional arbitrator."

[8] Participation Agreement Section 9.4 (App. 20a) provides: "All decisions reached by the Management Committee on matters concerning the South Texas Project and properly before the Management Committee for decision pursuant to the terms of this Participation Agreement shall be binding upon all Participants."

[9] The Participants set no fixed price for STP nor any deadline for its completion, and agreed to construct STP jointly and to share any risks and benefits in accordance with their respective ownership shares. Participation Agreement Section 14.2 (App. 20a) provides: "Each Participant shall pay its share of construction costs in accordance with requests for funds submitted by the Project Manager."

All parties recognized that both the Federal Arbitration Act, 9 U.S.C. § 1, et seq. (the "FAA"), and the Texas General Arbitration Act, Tex. Rev. Civ. Stat. Ann. article 224, et seq. (the "Texas Act"), are applicable. In proceedings before the trial court, HL&P asked that, if arbitration was required, the court restructure the panel in aid of fair arbitration (Appendix F). Article 235(G) of the Texas Act (App. 14a) provided the court plenary authority, in addition to its inherent equity powers, to grant such relief. HL&P asserted that requiring it to arbitrate before a panel whose majority had been appointed by claimants against HL&P violated its constitutional rights to due process under the Fourteenth Amendment to the Constitution, as well as its statutory rights under the FAA and the Texas Act.

HL&P pointed out that in *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968), this Court addressed "whether elementary requirements of impartiality taken for granted in every judicial proceeding are suspended when the parties agree to resolve a dispute through arbitration." The Court answered this question by holding that in the FAA Congress intended to provide not merely for *any* arbitration but for an impartial one (*id.* at 147), concluding that "any tribunal permitted by law to try cases and controversies not only must be unbiased but also must avoid even the appearance of bias." *Id.* at 150. Decision of claims against HL&P by a panel majority appointed by the claimants cannot meet the *Commonwealth* standard.

The district court did permit the addition of an arbitrator named by Austin, another claimant against HL&P (App. 2a). This addition did not elevate fairness above minimum levels, but exacerbated the problem. At that point there would be an even-numbered four-arbitrator panel, and the Participation Agreement requires election of a fifth member by the four. The addition of a fifth arbitrator would do nothing to prevent Austin, CPL and San Antonio from reallocating their respective costs in STP under the guise of a "damage" award by their appointed arbitrators.

Faced with this real and apparent unfairness in the composition of the panel, San Antonio, CPL and Austin attempted to repair it by having their appointed arbitrators sign a form of "neutrality oath" (Appendix L) similar to those required of neutral arbitrators by rules of the American Arbitration Association (Appendix K). These rules, however, are traditionally applied in "tripartite" arbitrations, in which each of the disputing parties appoints a panel member, and the inherent bias of party-appointed arbitrators is overcome by the deciding vote of the third neutral member. Appointees who know they were chosen by a party to a dispute cannot be considered "neutrals" in arbitration practice. See *infra* pp. 12-13.

Further, the arbitrators appointed by San Antonio and CPL are both ratepayers of the San Antonio electric utility and have a material financial interest in the outcome of the arbitration (Appendix M). As such they are disqualified under the doctrine of *Tumey v. Ohio*, 273 U.S. 510 (1927) from acting as judges in their own case. As the *Tumey* opinion states,

> There are doubtless mayors who would not allow such a consideration as $12 costs in each case to affect their judgment in it; but the requirement of due process of law in judicial procedure is not satisfied by the argument that men of the highest honor and the greatest self-sacrifice could carry it on without danger of injustice.

Id. at 532.[10]

Oaths by judges and jurors do not in and of themselves overcome issues of bias and disqualification; these elementary requirements for judicial proceedings are made applicable to judicial enforcement of arbitration agreements by *Common-*

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[10] Apart from pecuniary interest, San Antonio ratepayers share a community interest in achieving recompense for asserted misdeeds by HL&P which allegedly resulted in hundreds of millions of dollars in unnecessary costs. The arbitrators appointed by San Antonio and CPL can reasonably be expected to consider who appointed them in reaching their decisions, and to be influenced to adopt partisan positions. See *Tumey*, 273 U.S. 532-35.

wealth. Thus the "neutrality oaths" cannot cover up the basic unfairness of an arbitration panel.

The trial court nonetheless rejected HL&P's pleas, and ordered arbitration before a five-member panel composed of the respective appointees of San Antonio, CPL, Austin and HL&P, and a fifth to be elected by the four party-appointees (App. 2a). The court refused to restructure this panel in any way to aid arbitration and to thus satisfy the requirements of due process (App. 4a). Possible corrective steps included recognizing that there are two "sides" to the dispute, and equalizing the number of appointees by each side; directing arbitration of the separate disputes with HL&P by San Antonio and CPL by different tripartite panels; requiring new appointments from a panel of true neutrals using a procedure which prevents the designees from knowing who selected them; and other available remedies.[11]

Under Texas law, a trial court order staying litigation and directing arbitration is not appealable. *Citizens Nat'l Bank v. Callaway*, 597 S.W.2d 465, 466 (Tex. Civ. App. — Beaumont 1980, writ ref'd). However, Texas precedent recognizes that such an order is reviewable by mandamus under an abuse of discretion standard.[12] Hence HL&P sought leave to file mandamus in the Texas Court of Appeals, which was denied one day after it was filed (App. 6a). Leave to file mandamus was then sought in the Texas Supreme Court, and denied on June 19, 1991 (App. 7a). HL&P then sought rehearing, which was denied by the Texas

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[11] Remedies to ensure fair arbitration, such as those available but rejected here, have been utilized by other courts in comparable situations. See *infra* pp. 14-15.

[12] The Texas courts have recognized and exercised this authority repeatedly in arbitration cases. *Merrill Lynch, Pierce, Fenner and Smith, Inc. v. Longoria*, 783 S.W.2d 229 (Tex. App. — Corpus Christi 1989, orig. mand. proceeding); *Shearson Lehman Hutton, Inc. v. McKay*, 763 S.W.2d 934 (Tex. App. — San Antonio 1989, orig. mand. proceeding); *USX Corp. v. West*, 759 S.W.2d 764 (Tex. App. — Houston [1st Dist.] 1988, orig. mand. proceeding); *see also Mewbourne Oil Co. v. Blackburn*, 793 S.W.2d 735 (Tex. App. — Amarillo 1990, orig. mand. proceeding) (reviewing questions presented through mandamus, but denying relief).

Supreme Court on October 30, 1991 (App. 8a). In each instance the denial of mandamus was without opinion.

REASONS FOR GRANTING THE WRIT

I. This Case Presents Issues of National Significance

A. National Policy Favoring Arbitration Requires Fair Proceedings

Since deciding the so-called *Trilogy* labor arbitration cases in 1960,[13] this Court has supported a national policy favoring resolution of disputes by arbitration. In a series of decisions spanning three decades,[14] the Court has consistently supported Congressional policy, as expressed in the FAA, of enforcing agreements to arbitrate contractual disputes. The Court has thereby enhanced the viability of arbitration as an alternative to litigation, so that by 1985 Justice Blackmun could state with confidence: "[W]e are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution." *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626-27 (1985).

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[13] *United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593 (1960); *United Steelworkers of America v. Warrior & Gulf Navigation Co.*, 363 U.S. 574 (1960); *United Steelworkers of America v. American Manufacturing Co.*, 363 U.S. 564 (1960). The Court there held that doubts about enforcement of labor arbitration agreements must be resolved in *favor* of arbitration, departing from earlier decisions, such as *Wilko v. Swan*, 346 U.S. 427 (1953), where the Court found arbitration to be an inadequate substitute for litigation.

[14] *E.g., Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967) (limiting issues courts can examine when enforcing arbitration agreements); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974) (FAA puts arbitration agreements "upon the same footing as other contracts"); *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1 (1983) (FAA does not permit court to delay enforcement of arbitration agreement pending outcome of related state court proceeding); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987); and *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989) (overruling *Wilko v. Swan*).

Given the ever-increasing number of disputes courts are asked to decide,[15] "a national policy encouraging courts to enforce arbitration agreements remains critical. But that policy makes sense *only* if judicially-enforced arbitration will lead to resolution of disputes in accordance with fundamental principles of due process. Litigants cannot have confidence in arbitration proceedings that do not meet minimal standards of impartiality; nor can the outcome of such proceedings be respected.

B. Judicial Enforcement of Unfair Arbitration Violates Due Process

This Court's decisions in recent years have focused on issues of arbitrability. The issues in this case present a different aspect of arbitration; i.e., whether due process requires a fair panel before arbitration can be judicially ordered. It has been twenty-four years since this Court held in *Commonwealth Coatings v. Continental Casualty Co.*, 393 U.S. 145 (1968), that due process standards applicable to judicial proceedings are not suspended when arbitration is used as a substitute for litigation. Indeed, the Court in *Commonwealth* rejected the argument that fairness was somehow less important in arbitration proceedings than in litigation, stating: "we should, if anything, be even more scrupulous to safeguard the impartiality of arbitrators than judges, since the former have completely free rein to decide the law as well as the facts and are not subject to appellate review." *Id.* at 149.

The requirement that arbitration proceedings be impartial both in fact and in appearance has both statutory and constitutional underpinnings. The FAA reflects Congressional intent to provide "not merely for *any* arbitration but for an impartial one." *Com-*

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[15] *See, eg.*, Nat'l Law Journal, January 13, 1992, at 5, col.1 (reporting on increased caseloads and delays described in Chief Justice Rhenquist's "1991 Year-End Report of the Supreme Court and the Federal Judiciary").

monwealth at 147. In *Hines v. Anchor Motor Freight, Inc.*, 424 U.S. 554, 571 (1976), the Court affirmed this principle:

> Congress has put its blessing on private dispute settlement arrangements . . . but it was anticipated, we are sure, that the contractual machinery would operate within some minimum levels of integrity.

The constitutional basis for the holding in *Commonwealth* is found in the basic principles laid down in *Tumey v. Ohio*, 273 U.S. 510 (1927), which held that due process requires any tribunal deciding cases to be free of the appearance of partiality or financial interest. *Commonwealth's* application of these standards to arbitration panels remains critical today because of the increased use of binding arbitration as a surrogate for litigation.

The constitutional holding in *Commonwealth* has been widely followed. The New Jersey Supreme Court has held that "[t]he parties may agree to any form of dispute resolution that they wish, but they may not seek the backing of the courts for private actions that, while substituting for the judicial function, are fraught with the appearance of bias." *Barcon Assocs. v. Tri-County Asphalt Corp.*, 430 A.2d 214, 222 (N.J. 1981). The Michigan Supreme Court agreed that in arbitration as well as judicial contexts "[a] basic requirement of due process is a 'fair trial in a fair tribunal.' [citations omitted] Essential to this notion is a fair and impartial decisionmaker." *Morris v. Metriyakool*, 344 N.W.2d 736, 738 (Mich. 1984).

The actions of the Texas courts, which compel HL&P to arbitrate damage claims against it before an unfair panel controlled three-to-one by arbitrators chosen by its opponents, do not meet these statutory or constitutional standards. This Court's correction of those actions, including reaffirmation of the principles of *Commonwealth Coatings*, would not only result in compliance with due process requirements, but also facilitate and expedite arbitration proceedings by requiring that courts ensure at the outset that arbitral panels comport with due process stan-

dards. Through this means arbitration can and will be accepted as a fair and meaningful alternative to litigation.

C. Multi-Party Disputes Particularly Require Actions to Ensure Due Process

Contractual disputes arising under multi-party contracts cannot always be resolved fairly when each party appoints an arbitrator. Depending on the nature of the controversy, a panel which is unfair both in fact and in appearance can result from literal application of such a formula. The present case provides an example of such unfairness: the claimants against HL&P have appointed three arbitrators to HL&P's one. Even the selection of an additional neutral arbitrator would not correct the imbalance.[16]

The problem stems from the inherent bias of party appointees. Courts have long recognized "that the party-designated arbitrators are not and cannot be 'neutral' at least in the sense that the third arbitrator [in a tripartite panel] or a judge is." *Astoria Medical Group v. Health Ins. Plan*, 182 N.E.2d 85, 87 (N.Y. 1962). In fact, party-appointees "are expected by the disputants and should be understood by the courts to act as *partisans only one step removed from the controversy*," *Finkelstein v. Smith*, 326 So.2d 39, 40 (Fla. Dist. Ct. App. 1976) (emphasis added). They are "effectively, and *by design*, representatives of the respective parties," *Richco Structures v. Parkside Village, Inc.*, 263 N.W.2d 204, 210 (Wis. 1978) (emphasis added), who are expected to be "*advocates*" for each respective position, *Anderson v. Nichols*, 359 S.E.2d 117, 123 (W.Va. 1987) (emphasis added).

The arbitration rules of the American Arbitration Association ("AAA") recognize the practical realities of party appointment. Rules 12 and 19 of the AAA *Commercial Arbitration Rules* provide that party-appointed arbitrators are not disqualified because of bias (App. 26a). The ABA *Code of Ethics for Arbitra-*

[16] The additional fifth arbitrator could not be neutral unless selected unanimously by the four party appointees. The order of the district court does not impose this requirement of unanimity.

tors in Commercial Disputes (Appendix J) specifically recognizes that party-appointed arbitrators "may be predisposed toward the party who appointed them" and that their obligation to reach an "independent, just and deliberate" award may properly be tempered by this predisposition. (Canon VII A, E, App. 23a, 25a). Further, the disclosure and *ex parte* communications principles generally applicable to arbitrators are relaxed for party-appointees (Canon VII B, C, App. 23a-25a). While serving as arbitrators, such individuals are not barred from the sort of financial, business, professional, social or family relationships that are likely to affect impartiality (Canon VII A(2), App. 23a). In the typical "tripartite" arbitration, this predisposition by two party-appointed arbitrators is balanced by the neutral third arbitrator who casts the deciding vote.[17]

But this practical protection disappears when there are more than two parties to the arbitration who appoint arbitrators, and a neutral no longer controls the decision. The New York Court of Appeals addressed such a case in *Di Stasio v. Avallone*, 234 N.E.2d 255 (N.Y. 1967),[18] adopting the view that an arbitration by a panel composed of two arbitrators appointed by parties on one side of a dispute and a third by the opposing party "will be a mere sham and its determination a foregone conclusion." 277 N.Y.S.2d at 575. Common sense supports this conclusion; an arbitration before such a panel would not achieve the "elementary requirements of impartiality" or avoid the "appearance of bias" as mandated by *Commonwealth*.

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[17] The "Introductory Note" to Canon VII (App. 22a-23a) dealing with *tripartite* arbitration panels, explains the balancing process: "In such arbitrations, the two party-appointed arbitrators should be considered non-neutrals unless both parties inform the arbitrators that all three arbitrators are to be neutral, or unless the contract, the applicable arbitration rules, or any governing law requires that all three arbitrators are to be neutral." In both of these panels the presence of the third, neutral arbitrator assures an impartial decision, even if the party-appointed arbitrators disregard their promise to be impartial, because the neutral holds the controlling vote.

[18] The Court of Appeals adopted the dissenting opinion of Justice Steuer in the Appellate Division reported at 277 N.Y.S.2d 573 (App. Div. 1967).

The result here — three to one arbitration — is as much of a sham proceeding as in *Di Stasio*. Arbitration before such a panel does not comport with due process as required by *Commonwealth*.

D. Available Remedies In Aid of Fair Arbitration Should Be Employed by Courts Before Arbitration Begins

What, then, should a court do when asked to order arbitration before such an unbalanced panel? The answer lies in restructuring the panel, rather than in denying arbitration or sending the parties to arbitrate before a panel that fails to meet required standards. This is the action approved by the New York Court of Appeals in *Di Stasio*. The language of the arbitration clause was there interpreted to provide for the appointment of one arbitrator by each of the two *sides* of a dispute, with a third neutral selected by the two party-appointees. Thus the two defendants appointed one arbitrator, as did the plaintiff. Through this means the balance achieved by a "tripartite" panel was accomplished.

Judge Medina accomplished fairness by a different means, in *Compania Espanola de Petroleos, S.A. v. Nereus Shipping*, 527 F.2d 966 (2d Cir. 1975). Each of the three parties was permitted to appoint an arbitrator to a five-member panel, and the three party-appointees unanimously added two additional arbitrators. The court stated, "we are convinced that the method we have chosen is the only method that will give each of the parties fair and equitable treatment." *Id.* at 975.

Ample precedent further supports judicial intervention to correct an unfair panel *before* an arbitration occurs. *Erving v. Virginia Squires Basketball Club*, 468 F.2d 1064 (2d Cir. 1972) (arbitrator named in agreement replaced because he was a partner in the law firm representing party); *Cristina Blouse Corp. v. Int'l Ladies Garment Workers' Union*, 492 F.Supp. 508 (S.D.N.Y. 1980) (arbitrator named in agreement replaced because he had formerly represented the union); *Rabinowitz v. Olewski*, 473 N.Y.S.2d 232 (N.Y. App. Div. 1984) (Jewish trade organization named as arbitrator in agreement replaced because a

letter accusing party of PLO ties and crimes committed in Israel had circulated among the membership); *Elmarina, Inc. v. Comexas*, N.V., 679 F.Supp. 388 (S.D.N.Y. 1988) (following *Nereus, supra*); *Matter of Czarnikow-Rionda Co.*, 512 F.Supp. 1308 (S.D.N.Y. 1981) (following *Nereus, supra*). *See also Third Nat'l Bank v. Wedge Group, Inc.*, 749 F.Supp. 851, 855 (M.D. Tenn. 1990) ("Where the potential bias of a named arbitrator makes arbitration proceedings a prelude to later judicial proceedings challenging the arbitration award, a court can appoint a neutral substitute arbitrator").

The need for judicial action in the present case was triggered not only by the unfair imbalance of the panel, but also by the pecuniary interest of the two San Antonio ratepayers appointed by San Antonio and CPL. See the discussion at *supra* p. 7. Disqualification and replacement of these appointees by the court is required under *Tumey v. Ohio*, *supra*. The court could, of course, adopt a method of replacement which preserves the parties' contract right to designate an arbitrator, provided other steps are taken (such as those described above) to ensure that one or more neutrals who are not party-appointees control the decision.

II. Limited Review Under a Strict Standard After an Arbitration Award is not an Adequate Remedy to Correct an Unfair Arbitration Panel Which is Biased in Fact and Appearance

The Texas Act sets out two standards for review of an arbitral award for bias. The award will be vacated if an arbitrator "appointed as a *neutral*" displays "evident partiality." Art. 237(A)(2) (emphasis added) (App. 15a). A narrower standard applies for a party-appointed arbitrator: his actions must exhibit "corruption," prejudicial misconduct or "willful misbehavior" to justify reversal. *Id.* Both standards focus on the conduct of an individual. The insidious or inherent bias of an unfairly weighted panel is not addressed, although it is even more likely to produce a prejudicial award. Review standards under the FAA are

similarly limited. Under § 10 an award may be vacated for "evident partiality or corruption in the arbitrators, or either of them." 9 U.S.C. § 10 (App. 18a).

Neither the Texas Act nor the FAA addresses the problem of structural bias on an arbitration panel. If the *structure* of the panel is flawed, bias may be manifested only in a massive damage award against HL&P, and HL&P could have the difficult task of proving that the award was *necessarily* the product of an individual's "evident partiality" or "corruption." Statutory appeals thus provide only limited grounds for review which cannot assure a result consistent with *Commonwealth Coatings*.

Even if the award were vacated on appeal, HL&P would still be denied due process. This Court has recognized that there is an independent denial of due process where a litigant is subjected to trial by a biased tribunal and has refused to require parties to submit to unfair proceedings merely because their due process rights might be salvaged on appeal. In *Gibson v. Berryhill*, 411 U.S. 564, 577 (1973), for example, the Court found that where a quasi-judicial body "was incompetent by reason of bias to adjudicate the issues pending before it," a court "need not defer" and could intervene even though "judicial review, *de novo* or otherwise, would be forthcoming at the conclusion of the . . . proceedings." Similarly, in *Ward v. Village of Monroeville*, 409 U.S. 57 (1972), the Court held that adjudicative procedure could not

> be deemed constitutionally acceptable *simply because the State eventually offers a defendant an impartial adjudication. Petitioner is entitled to a neutral and detached judge in the first instance.*

Id. at 61-62 (emphasis added).

Here HL&P lacks even the prospect of delayed *de novo* review. The reality of arbitration before a partial and imbalanced forum, coupled with the narrow grounds for review afforded by the Texas Act and the FAA, argue *a fortiori* for intervention by this Court before under the doctrine articulated in *Berryhill* and *Ward*.

CONCLUSION

The Court should grant certiorari and set this case for argument. In an increasingly complex world, arbitration must be available as an alternative to litigation. Requiring at the outset that arbitration panels meet the requirements of due process will facilitate that ultimate goal.

Respectfully submitted,

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